

**Minutes
Investment Advisory Council
February 16, 2016**

The Investment Advisory Council (IAC) met at 12:00 P.M. on Tuesday, February 16, 2016 in the Board Room – First Floor, 60 Empire Drive, St. Paul, Minnesota.

MEMBERS PRESENT: Doug Anderson, Jeff Bailey, Dave Bergstrom, John Bohan, Dennis Duerst, Doug Gorence, Laurie Hacking, Gary Martin, Malcolm McDonald and Elaine Voss.

MEMBERS ABSENT: Denise Anderson, Kerry Brick, Kim Faust, Kristin Hanson (for Myron Frans), and Jay Kiedrowski.

SBI STAFF: Mansco Perry, LeaAnn Stagg, Paul Anderson, Patricia Ammann, Cassandra Boll, Nate Blumenshine, Tammy Brusehaver, Stephanie Gleeson, Inma Conde Goldman, Aaron Griga, Andrew Krech, Steve Kuettel, Mike Menssen, Mercy Ndungu, Jonathan Stacy, Robert Weiler, Charlene Olson and Melissa Mader.

OTHERS ATTENDING: Ann Posey and Rod Bare, Callan Associates Inc.; Bert Black, Christie Eller and John Mule, Attorney General's Office; Cumah Blake, Office of the Governor; David Kenney, Office of the State Auditor; Dave DeJonge, PERA; Jay Stoffel, TRA; Jim Mulrooney, Wells Fargo; Rick Baert, Pensions & Investments; Jim Baker, UNITE HERE; Edgar Hernandez, SEIU; John Fisher and Lonnie Duberstein, REAM; and Gordon Voss, private citizen.

The minutes of the November 18, 2015 meeting were approved.

Executive Director's Report

Mr. Perry referred members to Tab A of the meeting materials, and he reported that the Combined Funds had outperformed its Composite Index over the ten year period ending December 31, 2015 (Combined Funds 6.7% vs. Composite 6.5%) and had provided a real rate of return of 5.6% above inflation over the latest 20 year period (Combined Funds 7.8% vs. CPI 2.2%).

Mr. Perry said that assets increased over the quarter by 2.0% (Combined Funds ending value of \$57.9 versus a beginning value of \$56.7 billion), due to positive investment returns that outweighed net outflows. The Combined Funds return matched the benchmark for the quarter (Combined Funds 2.9% vs. Composite 2.9%) and was 10 bps higher for the year (Combined Funds 0.0% vs. Composite -0.1%). The Combined Funds also outperformed its benchmark for longer time periods.

Mr. Perry reported that the domestic stock manager group underperformed its target for the quarter (Domestic Stocks 5.9% vs. Domestic Equity Asset Class Target 6.3%), and underperformed for

the year (Domestic Stocks 0.3% vs. Domestic Equity Asset Class Target 0.5%), and had mixed performance over longer time periods. He said the international stock manager group outperformed its target for the quarter (International Stocks 3.8% vs. International Equity Asset Class Target 3.2%) and outperformed over longer time periods. Mr. Perry then stated that the bond segment outperformed its target for the quarter (Bonds -0.3% vs. Fixed Income Asset Class Target -0.6%) and for the year (Bonds 0.7% vs. Fixed Income Asset Class Target 0.5%) and also outperformed its target over longer time periods. He stated that the alternative investments detracted from performance for the quarter and contributed to performance for the year (total return of -1.9% and 1.4%, respectively). Mr. Perry concluded his report noting that, as of December 31, 2015, the SBI was responsible for managing slightly under \$80 billion of assets.

Mr. Perry referred members to Tab B of the meeting materials for the Executive Director's Administrative Report. Mr. Perry commented that the Fiscal Year 2015 audit was concluded and that the SBI received a clean, unqualified opinion. Mr. Perry also stated that the Fiscal Year 2015 Annual Report had already been distributed. Mr. Perry stated that Tab B contains the updated information for Sudan and Iran. Mr. Perry noted that the SBI is ahead of budget for the fiscal year, that the office remodel is finished, and that he does not anticipate spending all of the amounts appropriated for the year.

Mr. Bailey turned the meeting over to the SBI's Private Markets Team. Mr. Blumenshine gave a brief overview of the alternatives portfolio market value and cash flows for the prior quarter. Mr. Stacy, Ms. Boll and Mr. Krech described the six deals which were Apax Partners (Private Equity), Leonard Green & Partners (Private Equity), Strategic Partners (Private Equity), Angelo, Gordon & Co. (Real Estate), Carlyle Strategic Partners (Private Equity), and Rockpoint Group (Real Estate). The Investment Officers answered IAC member questions. Mr. McDonald moved approval of the six recommendations and Mr. Bohan seconded the motion. Ms. Hacking abstained from the vote stating that a family member is employed by one of the firms under consideration. The motion passed.

Mr. Perry introduced staff members Ms. Brusehaver, Ms. Gleeson, and Ms. Boll who provided an overview of the domestic equity, international equity, and fixed income markets during the fourth quarter.

Mr. Perry stated that in the next couple of quarters he expects to bring recommendations to the Committee with respect to domestic equity small-cap growth managers and emerging markets equity managers, areas where he feels there could be better performance. Mr. Perry also indicated that the SBI is working with Minnesota State Retirement System (MSRS) on the Defined Contribution program and that there may be some updates at the next meeting. Mr. Perry reminded the Committee that the meeting materials have been streamlined. Mr. Perry indicated that the manager commentaries, which are not regularly distributed, are available at any time upon request. Mr. Perry also stated that he expects to include the Value of Active Management (VAM) charts, and some additional quantitative manager information, in the report annually at the end of the fiscal year. Mr. Bergstrom asked if staff would be reviewing the percentage allocation to active and passive management in the Domestic Equity Program. Mr. Perry responded by saying that he still believes in active management, but thinks it should be focused on the less efficient areas of the market, for example small-cap domestic equities. Mr. Duerst asked Mr. Perry about his

thoughts on the high-yield markets and whether the Program has enough exposure to it through the yield-oriented private equity investments. Mr. Perry acknowledged that the Program's fixed income investments are core-oriented and that he thinks that there are other areas of the fixed income market that are worth looking at and investing in. Mr. Perry noted that he believes a credit bucket consisting of both public and private investments could be a feasible option. Mr. Bohan asked what priorities have been established for the fiscal or calendar year. Mr. Perry responded that at the next meeting Callan and staff will bring forth recommendations for action on asset allocation as well as other workplan items for fiscal year 2017.

Mr. Perry commented on the need to consider private investment opportunities outside the U.S. and introduced Melissa Ma of Asian Alternatives and Steven Cha of Angelo Gordon to lead a roundtable discussion on investment opportunities in Asia. Mr. Cha gave an overview of the private markets and private real estate opportunities in Asia and Ms. Ma followed up with an overview of opportunities in Asian private equity. Mr. Cha and Ms. Ma answered questions posed by the council members. Both speakers concluded with comments on how an investor can begin the process of developing an Asian segment in a private markets portfolio.

The meeting adjourned at 2:45 p.m.

Respectfully submitted,



Mansco Perry III
Executive Director and
Chief Investment Officer

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